

VZCZCXRO0243

RR RUEHCHI RUEHCN RUEHDT RUEHGH RUEHHM RUEHNH

DE RUEHGZ #0076/01 0410810

ZNR UUUUU ZZH

R 100810Z FEB 10

FM AMCONSUL GUANGZHOU

TO RUEHC/SECSTATE WASHDC 1371

INFO RUEHOO/CHINA POSTS COLLECTIVE 0459

RUCNASE/ASEAN MEMBER COLLECTIVE

RUEHBJ/AMEMBASSY BEIJING 1124

RUEHCN/AMCONSUL CHENGDU 0386

RUEHHK/AMCONSUL HONG KONG 0452

RUEHGH/AMCONSUL SHANGHAI 0385

RUEHSH/AMCONSUL SHENYANG 0395

RUCPDOC/DEPT OF COMMERCE WASHDC

RUEATRS/DEPT OF TREASURY WASH DC

RUEHC/DEPT OF LABOR WASHDC

RUEAIIA/CIA WASHDC 0427

RUEKJCS/DIA WASHDC 0423

UNCLAS SECTION 01 OF 03 GUANGZHOU 000076

SENSITIVE

SIPDIS

STATE FOR EAP/CM, EAP/EP, EEB/TPP, EEB/IFD, S/P, INR/EAP
STATE PASS USTR CHINA OFFICE

E.O. 12958: N/A

TAGS: [ETRD](#) [ECON](#) [KIPR](#) [EFIN](#) [EINV](#) [PGOV](#) [CH](#)

SUBJECT: Domestic Demand Strong, But Not "High End" in Guangxi's Industrial Center

REF: A) GUANGZHOU 75, B) 09 BEIJING 425, C) 07 GUANGZHOU 862

GUANGZHOU 00000076 001.2 OF 003

(U) This document is sensitive but unclassified. Please protect accordingly. Not for release outside U.S. government channels. Not for internet publication.

¶1. (SBU) Summary and comment: Demand for inexpensive automobiles and heavy machinery produced in Liuzhou, the main manufacturing city in the Guangxi Zhuang Autonomous Region, increased in 2009 and is likely to exceed sales records in 2010, according to local executives. However, China's domestic demand for the companies' costlier high-end products remains weak when compared with low- and mid-tier product lines. Tourism in Guilin, 80% of which consists of domestic travelers, was hurt by the economic downturn but showed a strong recovery in 2009 that local officials predict to continue in ¶2010. IPR protection has taken root as a priority for Guilin officials, but work remains to be done before the city can truly live up to the central-government conferred title of "Model IP City." End summary and comment.

¶2. (SBU) South China's third-tier economic growth was on display during the Consul General's February 1-3 visit to Guilin and Liuzhou, Guangxi Autonomous Region's most important cities for tourism and heavy manufacturing. Guilin Vice Mayor He Liangjun told the CG that despite being designated as a national-level tourism center (along with Beijing and Xi'an), the 2008 economic slowdown, and a corresponding decline in the number of visitors, was difficult for his city's tourism industry. Separately, Liuzhou Mayor Zheng Junkang remarked that the effects of China's economic stimulus paid handsomely for his city's three most important industries -- steel, automobiles and construction equipment. Both leaders, as well as their department-level officials, expressed optimism that robust economic growth will continue in 2010 following a strong year in ¶2009.

Economic Stimulus, Guilin- and Liuzhou-style

¶3. (SBU) Infrastructure projects in both Guilin and Liuzhou were ubiquitous before the economic downturn, but China's infrastructure-focused economic stimulus bolstered each city's efforts in 2009, according to city leaders. Water treatment and

distribution, new roads and bridges, and expansion of green areas were common themes highlighted by officials who met with the CG on February 2 and 3. (Meetings with NGOs, educators, and the press reported in ref A.) Guilin, which claims 40% of its urban areas are forested, has focused on reducing pollution caused by garbage and waste water, according to Vice Mayor He. Governing an industrial city, however, Mayor Zheng said Liuzhou's designation as one of four Chinese cities with acid rain is being addressed through physical improvements to the water sewage system as well as efforts to reduce emissions from heavy industries.

Boom Times for Heavy Manufacturers in Liuzhou

¶4. (SBU) General Motors operates a 13,000 employee joint venture automobile plant (partnering with Shanghai Automotive Industry Corporation and Wuling Motors) in Liuzhou that became the first in China to exceed annual production of one million vehicles in 2009. The plant already has two vehicle plants and a two-year old engine plant in operation, but Vice President Matthew Tsien said it still had trouble keeping up with burgeoning demand in 2009 and is currently expanding production in order to meet projected 2010 sales for inexpensive small-sized minivans and entry-level compact cars. The factory's small-sized minivan, known locally as the Wuling Sunshine, is a market leader in China, with just under 50% market share nationwide. Tsien said the company began production of a locally-designed mid-sized minivan that competes in a higher-end market segment and is produced at the joint venture company's Qingdao factory. The government announced an incentive program commonly known as "Cars for the Countryside" in March 2009, which Tsien said was a major factor in the Liuzhou GM factory's 67% sales increase last year. The policy offered subsidies to rural purchasers of small-displacement vehicles (engines under 1.6 liters) like those produced at the Liuzhou GM factory. (Note: More detailed

GUANGZHOU 00000076 002.2 OF 003

information about the program can be found on the following website: http://www.gov.cn/zwgk/2009-03/20/content_126_4324.htm. End note.)

¶5. (SBU) Construction and heavy machine builder Liugong Machinery also saw an increase in tractor and other equipment sales in 2009, Vice President for Research and Development David Beatenbough told the CG on February 3. However, even as domestic sales improved, overseas orders fell dramatically when construction projects were cancelled or delayed during the global economic downturn. For Liugong, Beatenbough said the overseas sales decline hurt the company's plans for international expansion but not the bottom line because the company only relies on overseas markets for 15% of its annual revenue. Liugong employees described subsidies very similar to those seen for many of China's export industries, including VAT rebates (ref B and C) and tax incentives for domestic R&D expenditures. More important than the subsidies, continued growth in China's domestic construction sectors served by Liugong were a boon to the company as it works to become a world leader in modern heavy machinery.

Domestic Demand Strong, But Not "High End"

¶6. (SBU) When asked to predict how the domestic market will look in 2010 and 2011, executives from both General Motors and Liugong said they expect to break new sales records in this timeframe. However, when asked about local R&D and introduction of higher-end technologies, GM's Tsien said, "Consumers would love to get more high-tech features and higher-end products, but they absolutely don't want to pay for it." Liugong executives offered a similar view, telling the CG that advanced Cummins engines are only used in certain equipment models designed specifically for export; almost all domestic customers insist on low-to-mid level products in terms of both price and features. By producing less expensive products to meet domestic demand, both firms had achieved rapid sales growth and profits, but not with the high margins that products from western countries and Japan regularly fetch in advanced markets.

Tourism Remains Key for Guilin

¶7. (SBU) Tourism, to the tune of 6 million visitors annually, is the main economic driver in Guilin city and surrounding areas with its population of just over one million people. International tourists from Asia, Europe and the United States account for 20% of the total visitors. Deputy Director Chen Yunchun of the Guilin Tourism Bureau told the CG that 60,000 U.S. tourists visit the city each year, and the city is ranked seventh in China for the number of international visitors each year. The economic downturn led to a 24% decrease in the number of 2009 visitors, but tourism picked up at the end of the year and 2010 will see growth return to prior levels, said Chen.

IPR Also Important to Guilin

¶8. (SBU) Protecting intellectual property rights (IPR) is increasingly a focus of Guilin's municipal government, according to an interagency group of working-level officials. Representatives of the Guilin Intellectual Property Office (IPO), Administration of Industry and Commerce (AIC), Economic Crimes Investigative Division (ECID) of the Public Security Bureau (PSB) and the Foreign Affairs Office (FAO) told the CG that resources for IPR enforcement have steadily increased in recent years. Guilin has established a government-wide interagency task force as well as IPR points of contact in the city's five urban districts and 12 rural counties. Enforcement efforts could receive even more attention if a proposal to certify the Guilin Municipal Court to handle IPR cases is approved, the officials said.

¶9. (SBU) Guilin's industrial development has expanded into pharmaceutical and medical products, leading to a concurrent increase in local counterfeit production. ECID officials took the opportunity to brief the Consulate on the recent case involving counterfeit Johnson & Johnson diabetic test strips. The investigation into the case was concluded in 2008 and is currently awaiting a final court decision and sentencing. Comment: Despite a

GUANGZHOU 00000076 003.2 OF 003

number of delays in the trial phase, the case could be an important example of successful IPR enforcement in south China. If the trial ends in jail time for the accused, which the law allows up to 7 years in this case, many observers and U.S. rights holders will see this case as an enforcement success. However, if it ends in administrative fines or suspended sentences, rights holders will see this as "business as usual" and continued weak enforcement of IPR that is endemic throughout much of south China. End comment.

GOLDBECK